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SPECIAL PAPER TWENTY-EIGHT

# **REGIONAL INTEGRATION AND TRADE LIBERALIZATION IN SUB-SAHARAN AFRICA**

**AN AERC COLLABORATIVE RESEARCH PROJECT  
Summary Report 1996**

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**POUR LA RECHERCHE ECONOMIQUE EN AFRIQUE**

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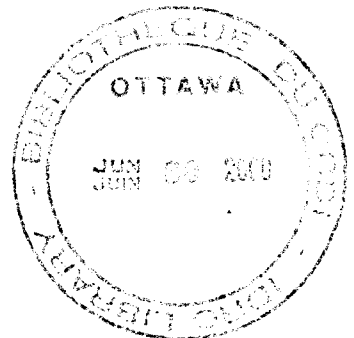
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## Preface

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The AERC Research Programme encompasses several types of research projects in order to suit the needs of the Programme, the researchers and the various themes they are investigating. One of these types is the Collaborative Research Project, which entails joint research by a team of African and non-African researchers coordinated by a senior African scholar on a mutually agreed theme. The collaborative approach is designed to produce a critical mass of high quality policy-oriented research. It is also an avenue for African scholars to exchange their experiences with counterparts elsewhere and to enhance skills.

The subject of this special paper is a summary of a Collaborative Research Project on Regional Integration and Trade Liberalization in Sub-Saharan Africa coordinated by Prof. T. Ademola Oyejide of the University of Ibadan, Nigeria (please see the annex for the complete list of contributors). The project yielded four volumes of material that are being published by Macmillan, London. The first volume is available from Macmillan and the remaining three volumes are due out in the coming year. This summary touches on the overall issues addressed, the findings and the recommendations. The material was also presented at a Dissemination Meeting for policy makers from sub-Saharan Africa held in Addis Ababa, Ethiopia in 1996 sponsored by the UNECA and the AERC. A report of that meeting is also available upon request from AERC.





# 1. Introduction

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This report describes the collaborative research project on Regional Integration and Trade Liberalization in sub-Saharan Africa, including an articulation of its key components and objectives. The report identifies and discusses the issues the project focused on, the major findings and results of the research, and the principal conclusions and their policy implications. The project was conceived and implemented in the context of the collaborative research modality of the African Economic Research Consortium (AERC). As part of AERC's publication and dissemination efforts, moreover, each of the various research reports has been or will be published individually, while the overall components are being issued in a four-volume series by MacMillan Publishers, London (see Annex). The formal launch of the project, at the May 1993 AERC workshop in Cape Town, followed several consultative meetings in various locations in and outside Africa.

In addition to AERC, sponsors of the project are Ford Foundation, the European Union, United Nations Development Programme and the Government of The Netherlands.

## ***Collaborative framework***

The main objectives of the collaborative research modality, which have also been reflected in the Regional Integration and Trade Liberalization Project design and implementation, include the following:

Within this collaborative framework, the project drew from the pool of researchers and resource persons in the networks of AERC and its collaborating partners. These partners include the Centre for the Study of African Economies, Oxford University; the Centre for Research on Economic Development and International Trade, University of Nottingham; the Development Economics Research Centre, University of Warwick; and the Centre for Economic Policy Research, London. The many individual researchers who participated are listed in the Annex.

The collaborative framework for this project used joint and interacting teams of researchers and resource persons drawn from networks organized around several African and non-African institutions. In constructing the various research teams, African researchers were consciously paired with their international counterparts to

optimize their respective comparative advantages with particular reference to technical tools and access to and understanding of the African policy community. The interactions were further enriched through periodic meetings of all the players to present, discuss and exchange ideas on draft papers at various stages of the research process. These meetings were also attended by selected members of the policy community from Africa and beyond (particularly the multilateral and bilateral donor agencies with special interest in Africa) whose experience and expertise positively influenced both the design and implementation of the research project.

The project comprised two major components. The first consists of a set of framework papers that set the stage for and guided subsequent parts of the project. The framework papers articulated the major research and policy issues, reviewed and assessed the existing knowledge base with regard to these issues, identified and developed appropriate research methodologies, and tentatively indicated some broad policy implications.

The second component of the project used case studies as the vehicle for the empirical analyses of the issues articulated by the framework papers. This component has two distinct but closely interwoven parts; one contains case studies of a sample of countries and the other consists of regional case studies.

The case study countries were carefully selected on the basis of criteria that reflect their geographical location, membership in a particular integration scheme, size and level of development. The ten countries are Côte d'Ivoire, Ghana, Kenya, Mauritius, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe.

The regional case studies cover six regional integration schemes: the Economic Community of West African States (ECOWAS); the Communauté Economique de l'Afrique de l'Ouest (CEAO) together with its successor, the Union Economique et Monétaire Ouest Africaine (UEMOA); the Union Douanière et Economique de l'Afrique Centrale (UDEAC); the Preferential Trade Area for Eastern and Southern Africa (PTA), together with its new manifestation, the Common Market of Eastern and Southern Africa (COMESA); the Southern African Development Coordination Conference (SADCC), recently transformed into the Southern African Development Community (SADC); and the Southern African Customs Union (SACU). Also included in the regional case studies is an analysis of unrecorded cross-border trade and trade flows in sub-Saharan Africa.

## ***Highlights of findings***

Despite the enthusiastic rhetoric in favour of regional integration arrangements in Africa, in general, it is safe to say that these schemes have not been particularly successful. In fact, the studies indicate that the least significant stimulus for trade liberalization—improved trade is one of the major objectives of such schemes—is

membership in a regional integration arrangement. While it appears true that trade in the region is naturally low, and not only because factors work against it, the shape and implementation of most of the integration schemes studied actually constrain trade.

Consensual decision-making arrangements, overlapping and often conflicting integration scheme memberships, lack of regional level monitoring of the implementation of decisions, unwillingness of governments to cede authority to the regional bodies, and subsequent lack of power by the regional secretariats to take initiatives have rendered the schemes impotent. The absence of effective compensation arrangements in many of the regional integration schemes has further hindered implementation of certain trade liberalization measures.

In many cases the chosen integration instruments were virtually guaranteed to discourage rather than promote intra-regional trade. With respect to ECOWAS and the PTA/COMESA, non-compliance with or delayed implementation of agreed liberalization schedules obviously did not enhance intra-group trade expansion. The domestic policy stance in these countries has also been generally at variance with the ideals of regional integration. In CEAEO, the key regional integration instrument is the regional cooperation tax (TCR), which contributes to the erosion of the international competitiveness of the integrated area. The common external tariff (CET) and the single tax (*taxe unique* or TU) put in place by UDEAC resulted in differential protection. SACU's key integration instrument is a revenue-sharing formula that has elicited grumblings from both the smaller members and the large South African economy.

National level trade liberalization, however, shows more promise, as liberalized trade regimes in a number of the individual countries studied correspond with improved economic indicators. The most dominant among the stimuli for trade liberalization noted in the case studies are linked to conditions imposed by structural adjustment programmes. The other side of this is that some trade reforms lack credibility because they are observed to be donor-driven and thus subject to reversal upon the whim of the government.

The reluctance of governments in some of the countries to refrain from using traditional trade policy instruments for addressing issues of macroeconomic incompatibility made policy reversals virtually unavoidable. Exchange rate adjustments appear crucial in this respect, as it is only with foreign exchange liberalization that the tariff structure becomes the principal source of protection.

The studies indicate that liberalization should not be construed as complete lack of trade controls. Some degree of protection is necessary as part of the proactive measures aimed at encouraging the expansion of the region's manufacturing sector. The level of import protection should be moderate, strictly limited, time bound, and related to some clearly understood and measurable performance standard. Thus, the immediate focus of policy attention should be on encouraging exports, while leaving

major import liberalization attempts until later. A successful, sustainable import liberalization programme requires successful exports.

The achievement and continuous maintenance of macroeconomic balance and stability are essential to successful trade liberalization. Lack of credibility of reforms is a major factor in the lukewarm performance of many liberalization attempts. African governments need to establish appropriate mechanisms for enforcing the policy restraint necessary for macroeconomic stability. Such an agency of restraint could take a number of forms, all of which require careful consideration and study before implementation:

1. Each country could use the regional scheme as an agency of restraint; this would require considerable strengthening of the schemes, as at present the penalties they can impose for breaking an agreement are small.
2. Credibility would be enhanced if tariff ceilings were “bound” under provisions of the GATT/WTO agreements, which can be used as an agency of restraint that would be effective against internal lobbying for policy reversals. African governments have not yet done so, having failed to take advantage of the opportunity offered by the Uruguay Round.
3. African customs unions could be linked to the European Union in fully reciprocal free trade arrangements. Such arrangements would have to be carefully considered, as there could be implications of “recolonization” of Africa, and costs/benefits need comprehensive analysis.

One picture does emerge: economies that are willing and able to participate in the global marketplace have been the most dynamic. Globalization offers important opportunities for accelerating economic growth all over the world. Countries and regions of the world that are unable or unwilling to integrate themselves into this emerging mainstream of the global economy might not benefit from the growth-enhancing features of globalization. In fact, the African experience suggests that inadequate integration into the world economy and consequent lack of growth have led to the region’s marginalization in the world goods and capital markets. That is not to say that globalization is free of problems. It can generate potentially severe and world-wide macroeconomic turbulence. It does not necessarily offer the same potential opportunities to all countries and the costs may also be differentiated. However, the more open economies in these case studies grew faster than the closed ones, while structural change corresponding to a shift in reliance from primary production to manufacturing occurred faster in open economies than in the relatively more closed ones.

In summary, while trade liberalization efforts in Africa do often show positive results, African regional integration schemes have not met expectations. They suffer from design and implementation problems, and their potential will not be realized until both of these problem areas are appropriately addressed.

The remainder of this report presents the details of the studies and their findings. Sections 2 and 3 define the problem on which the project was focused, articulating the scope, coverage and objectives of the project and analysing the theoretical relationships and empirical conjectures upon which the project was based. A review of experiences follows, with regional integration in Section 4 and then trade liberalization in Section 5. The final sections offer some ideas and suggestions for the way forward. Section 6 looks at issues and options regarding opening up and linking Africa together, while Section 7 does the same with regard to opening up and linking Africa with the world.

It is well to note that the views expressed here and in the project publications do not necessarily reflect the official position of AERC, the funders of the project or the collaborating institutions.

## **2. Project focus and objectives**

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This project began with the recognition that after more than three decades of experimentation, Africa's romance with regional integration continues unabated. It seems, in fact, to have intensified since the early 1980s. To underpin this continued interest, the Lagos Plan of Action offered a grand design that envisioned an evolutionary build-up from smaller regional groups in the western, central, northern, eastern and southern parts of Africa that should culminate, eventually, in an African Economic Community. The plan for this pan-African regional integration scheme was agreed to by the Organization of African Unity in 1980; the treaty was signed in June 1991.

Until recently, regional integration schemes in Africa developed largely as groupings of geographically contiguous countries, each of which operated primarily as a closed economy under the constraints of import-substitution industrialization strategies. Not surprisingly, perhaps, these regional integration efforts have generally achieved little success. In particular, there was limited recorded intra-group trade.

Several studies have identified a number of factors that may account for this failure. Participating countries generally fail to carry out agreed undertakings to abolish or even reduce trade barriers, probably because these regional undertakings are inconsistent with national-level import substitution policies or because they generate fears of unacceptable losses of tariff revenues. It appears that while African political leaders and their constituencies recognize the possible benefits that integration may bring, inaction is not necessarily viewed as an obstacle to progress in this matter. In general, the trade structures of participating countries are dominated by primary commodities and, hence, these countries are not necessarily each other's best trading partners. Finally, all the regional groupings have faced difficult distributional (gains and losses) questions for which no workable and mutually satisfactory compensation schemes could be designed.

The adoption of World Bank assisted structural adjustment programmes (SAP) by the large majority of African countries from the early 1980s is gradually leading to marked policy shifts away from predominantly import-substitution strategies and toward more open trade regimes. However, the SAPs and the trade liberalization

policies embedded in them were apparently designed and are being implemented without reference to the existing regional integration arrangements. It is thus not clear that the trade liberalization policies formulated by individual African countries are consistent with the undertakings these countries have entered into in the context of the integration schemes to which they belong. It is abundantly clear, however, that the continuing political rhetoric of African leaders regarding the issue of regional integration is profoundly out of step with the actual policy steps being taken at the level of individual countries.

This state of affairs raises a number of questions. What, for instance, is driving current regional integration discussions and efforts in Africa given the dismal experience over the last three decades? Is it to attract donor sympathy and funds? Is it because other parts of the world (notably Europe and North America) are building trading blocs? Or it is because the ongoing political opening-up sweeping across Africa combined with the SAP-induced trade liberalization is expected to provide a more conducive environment for a more successful regional integration effort?

Several other relevant questions are worth asking. How would regional integration under restructured economies differ from integration under protective structures? Would changes in trade barriers and outward orientation have significant implications for regional integration efforts? In principle, increased outward orientation may be expected to make countries more willing to implement agreed trade barrier reduction policies in the context of regional integration; the resulting trade liberalization may, in turn, directly boost actual intra-group trade, assist in changing trade structures and thus also boost potential intra-group trade. In this context, it becomes important to explore the analytical and policy implications of replacing a set of closed national economies with a closed regional economy.

Trade liberalization is at the heart of the structural adjustment and macroeconomic policy reforms embraced by most African countries since the early 1980s. Yet it has been relatively little studied, either on its own or, more importantly, in the context of existing regional integration efforts. In addition, little is sufficiently understood, in concrete terms, regarding the degree, instruments, sequencing and consequences of trade liberalization in African countries. Similarly, there is a lack of knowledge about the links between regional integration and trade liberalization, especially how and the extent to which SAP-induced trade liberalization hinders or enhances regional integration.

This project attempts to satisfy the need for a comprehensive study that would apply new perspectives and approaches, in terms of analytical framework and methodology, to the analysis of Africa's regional integration schemes and trade liberalization efforts, as well as the links between them. The focus and objectives are not limited to questions directed primarily at exploring Africa's past and current experience with regional integration and trade liberalization, important as these no doubt are. The project is also forward looking in the sense that it seeks to identify and

evaluate Africa's menu of future policy options regarding regional integration and trade liberalization. There is particular concern in the project for whether and the extent to which integration and liberalization processes could constitute viable mechanisms for opening up Africa, linking the continent together and linking it with the rest of the world as a means of enhancing sustainable growth and development.

Against the background of the general objectives, key issues and questions described above, the case study component of the project explores a number of more specific and empirical questions. Since there are two types of case studies and the issues they address are different, it is sensible to treat them separately and sequentially.

### ***The regional focus***

The project uses the case studies of African regional integration experience as a vehicle for posing and answering four key questions:

- What has been the performance of African regional integration schemes given their objectives, targets, main obstacles and constraints?
- What are the implications of changing economic and political conditions for regional integration in Africa?
- What is the impact of the global environment on African regional integration?
- What are the special issues of significance for particular regional integration schemes in Africa and how have they influenced the schemes to which they relate?

The first question seeks a firmer and more comprehensive understanding of African regional integration experience. This way of posing the question subsumes several important dimensions. Among these is the need to recognize and analyse the initial conditions such as potentials for market integration and the complementarity of production and trade structure of member countries that can be expected to affect eventual performance of regional integration schemes. Similarly, constraints to performance, such as existing barriers to trade and factor mobility between member countries, could have impacts that vary over different integration arrangements. Finally, implementation modalities and institutional designs often have significant implications for resolving distributional conflicts and managing compensation arrangements, which, in turn, could influence overall performance of regional integration schemes.

African political and economic policy landscapes have clearly undergone marked changes, particularly since the early 1980s. On the economic policy front, various



policy reforms have addressed issues of macroeconomic stabilization and structural adjustment, which include unilateral trade and financial liberalization, privatization, deregulation, and investment facilitation. These changing economic conditions influence intra-group trade and overall investment flows both across the various regional integration schemes and continent wide. Changes in the political arena that move in the direction of more transparent governance, democratization and greater participation in the political process can also be expected to enhance the growth of trade both within specific integrated areas and overall.

Changes in the global environment, particularly those that define the “rules of the game” under which trade and investment relations between countries are managed, have important implications for regional integration and trade liberalization in Africa. In particular, the completion of the Uruguay Round of multilateral trade negotiations and the establishment of the World Trade Organization (WTO) impinge upon the incentives for switching between regional and multilateral approaches to trade liberalization. Global liberalization under the auspices of the WTO would clearly affect regional integration through its impact on the margin of preferential tariffs that can be bargained among members of particular regional integration schemes.

Under the fourth question, the project seeks to explore how and the extent to which peculiar design features or orientations of certain regional African integration schemes may have influenced their performance. One example of a peculiar design feature of particular relevance is the role of France as “external anchor” for both CEAO and UEMOA; in the case of SADCC, confrontation against apartheid South Africa provided a special orientation and donor support that probably influenced the organization’s performance.

### ***The country focus***

Just as the project uses its regional case studies to explore a number of issues, it also uses the country specific case studies of trade liberalization experience to answer several questions, including the following:

- Has trade liberalization taken place?
- Are there linkages between particular episodes of trade liberalization and regional integration?
- Are specific trade liberalization episodes credible or not?
- What are the short-run and long-run consequences of particular trade liberalization episodes?

In answering the first question, the project defines trade liberalization in terms of several objective and quantifiable indicators such as changes in policies and observed changes in prices and quantities. These measures are then analysed to determine whether or not trade liberalization took place and, if so, when and over what period of time. In addition, the analysis of policy changes associated with price and quantity indicators of trade liberalization helps identify the main features of each episode of trade liberalization. The second question relates to linkages between regional integration and trade liberalization. It seeks to unravel two puzzles.

One is whether specific trade liberalization episodes occurred unilaterally or in the context of liberalization schedules negotiated and agreed upon between partners in a regional integration arrangement. The other is the extent to which commitments made by countries within their regional integration schemes are consistent with the trade liberalization decisions they make individually at the national level. In other words, this question seeks to determine whether regional integration and country level trade policy enhance or hinder each other.

The third issue relates to the credibility of particular trade liberalization episodes, which has been questioned in many African countries. This stems from a history of policy reversals implying specific unsustainable policy initiatives or incompatibility with other policies or developments in the economy. In assessing the credibility of each trade liberalization attempt this project develops and uses a series of diagnostics not only to determine credibility but also to indicate the proximate causes of credibility failure, when it occurs.

If trade liberalization episodes are credible and sufficiently durable private economic agents may be expected to react appropriately, and one may expect to see some short-run and long-run consequences. This is the set of issues that the fourth question of the country case studies of trade liberalization is intended to explore. In answering this question, each country case study analyses time series of output, employment and investment as well as the growth and composition of external trade as a means of measuring the short-run and long-run impacts of trade liberalization.

### **3. Background**

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Promotion of regional trade is an important objective of most of the regional integration schemes in Africa. However, trade expansion is not necessarily desired for its own sake but rather as a means to an end. In particular, accelerated development through increased regional trade has clearly been central to the vision of regional integration in Africa.

It is important, therefore, to explore the linkages and mechanisms through which regional integration is expected to bring about both an expansion of intra-regional trade and accelerated development of the integrated area essentially by liberalizing trade within the region.

Up to the early 1980s, most African countries tried to accelerate their economic growth on the basis of an import-substitution industrialization (ISI) development strategy. From the economic perspective, the small size of the typical African economy and the perceived disadvantages of smallness in the context of this strategy appear to be a key reason for the establishment of various regional integration schemes. In particular, a small population combined with low per capita income restrict the ability to benefit from lower unit costs arising from the exploitation of economies of scale and curtail allocative efficiency gains that could be generated by increased competition.

Against this background, regional integration appears to be a logical way to enable an economy to produce at lower unit costs for a larger (regional) market. Regional integration is embraced primarily as a means of widening market size and thus realizing the benefits of greater specialization and economies of scale. In this sense, import substitution in the context of larger regional markets could generate greater competition within the region and induce higher levels of productivity overall than were possible within the narrow confines of individual national markets. Compared with global liberalization, regional integration could be regarded as a more viable source of the benefits of economies of scale because of the anticipated problems of market access and the presumed higher transaction costs of producing for the world market.

The above notwithstanding, the arguments for regional integration do not lend themselves to unambiguous conclusions. At the static level and in the context of the simplest models, the desirability of an integration scheme depends on the balance of the opposing forces of trade creation and trade diversion. The case for regional

integration in the context of an export promotion strategy becomes stronger when dynamic factors are taken into account. However, whether this can be realized in practice depends on the extent to which economies of scale and international competitiveness are achieved, and on the feasibility of setting up a suitable compensation scheme, a key issue given the likelihood that effective regional integration could result in geographic concentration of certain economic activities (e.g., production facilities) within the integrated region.

Insights from new economic geography suggest that the interplay of economies of scale and location-specific costs could provide a rationale for regional integration schemes in Africa. The basic idea is that location decisions of producers are based on considerations of internal economies of scale and “trade costs”. Trade costs consist generally of transport and information costs (the latter include language and cultural barriers to ease of transactions). These costs increase with distance between the producer and the consumer. The inherited colonial pattern of production and trade between the typical African country and its European “mother” country combined with high trade costs between African countries has generated a “hub-and-spoke” trade pattern in which activities that have powerful scale economies, such as manufacturing, are located in the European “hub” from which they supply consumers located in numerous African “spokes”. In this arrangement, no African country “spoke” has a sufficiently large market to warrant the location of manufacturing production facilities in it unless trade costs within Africa can be drastically reduced.

A regional integration scheme that joins the spokes by reducing intra-African trade costs could radically alter the existing hub-and-spoke production and trade pattern and justify the location of production within the integrated region. The same location theory suggests, however, that if intra-regional trade costs are initially high, small reductions would tend to increase regional concentration of production. Clearly, this would generate greater inter-governmental conflict over compensation arrangements. Happily, though, the theory predicts that more sweeping and deeper liberalization measures that bring about large reductions in intra-regional trade costs might substantially counter the trend towards concentration of production. Thus, this analytical perspective not only provides a robust justification for regional integration in Africa, it also predicts that such a scheme would be more effective and less contentious if impediments to trade within the integrated region were quickly eliminated.

The third source of insights for constructing an economic rationale for regional interaction in Africa is the “agency of restraint” paradigm. This starts from the observation that, in Africa, government policies are frequently reversed. These policy reversals create credibility problems: private economic agents are reluctant to make investment and production decisions for fear of losses that could result from the reversals. Governments, on their part, can reverse policies easily because they are not subject to agencies of restraint that are sufficiently powerful to impose penalties

severe enough to deter such behaviour. In this context, the purpose of regional integration would be to promote investment and thus enhance economic growth by helping to enforce the policy restraint necessary for macroeconomic stability. What is required here is a participatory, reciprocal and supranational agency of restraint that ties key national economic policies in a reciprocal threat-making arrangement. The agency would ensure that all participating countries commit to sound and stable policies and should be in a position to effectively threaten errant members with credible and costly sanctions. Such an organization would have clear advantages over the essentially alien, unidirectional and unreliable “conditionality” of donors and international financial institutions.

In summary, analytical insights drawn from various theoretical perspectives suggest a number of propositions regarding regional integration and trade liberalization in Africa. First, some support and rationale can be found for regional integration in Africa. Second, however, one may have to look beyond the promotion of intra-regional trade as the key motivation for establishing regional integration. Third, regional trade is in any case unlikely to emerge as an important engine of African growth in the near term since African countries lack the income levels and structural complementarities that could generate large gains from regional specialization, whether within or across industries. Fourth, even if increased intra-African trade in the context of regional integration is viewed as intrinsically desirable, it may be best achieved as an automatic by-product of a more generalized rather than preferential reduction of trade barriers. Fifth, an African regional integration scheme motivated by the goal of avoiding the hub-and-spoke effects of inherited colonial production and trade patterns would be feasible and would be devoid of intense inter-governmental conflicts over compensation arrangements only if it is accompanied by rapid elimination of trade impediments in the integrating area that precludes geographical concentration of production facilities. Finally, perhaps the strongest argument for regional integration in Africa derives from the need to create a web of reciprocal deals and threats, supervised by a participatory supranational agency of restraint that increases the penalties for national-level policy reversal and so reduces its likelihood.

## **4. Regional integration experience**

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The analysis of the experience with regional integration in Africa is based on case studies of six regional integration arrangements. Two of these are CEAO/UEMOA and ECOWAS in West Africa; the Central African representative in the sample is UDEAC; and from eastern and southern Africa are SADC, PTA/COMESA and SACU.

The case studies cover a set of common issues and questions intended to provide a comparative framework for the analysis. The analysis focuses on the establishment and evolution of each regional integration arrangement, bearing in mind its antecedents, subsequent treaty reforms and revisions, and any transformations that may have taken place in terms of name, objectives, mandate and membership. Next, the analysis describes and interprets each regional integration scheme's motivation and objectives with a view to pinpointing the set of objectives that is either shared by all such schemes or can, in some other way, be regarded as dominant.

The third focus of the analysis relates to the broad characteristics of each regional integration arrangement. This covers the number of member states as well as the differences and similarities among them in terms of their economic and trade structures, their income levels, language, and colonial history. Next is a review of the institutions and instruments designed, established and used by each regional integration scheme as a means of achieving its objectives. Subsequently, the analysis examines each organization's main constraints as a prelude to a review of its performance. Following this is an attempt to more fully understand the implications for each regional integration scheme of the changing political and economic conditions in Africa since the mid 1980s, as well as the current and probable future impact of the global environment. Finally, the analysis reviews the relationship(s) between various regional integration schemes and the extent to which these relationships may enhance or hinder their performance.

### ***Establishment and evolution***

Several of the regional integration schemes have roots in much older colonial arrangements. Thus, although SACU was established in its present form only in 1969, it stems directly from the 1910 agreement between South Africa and the three British

High Commission Territories of Basutoland (now Lesotho), Bechuanaland (now Botswana) and Swaziland. Similarly, while the treaty establishing UDEAC was signed in 1964, it was in reality an outgrowth of UDE, which was created in 1959, and the Preferential Trade Area established in 1961 between Cameroon and the UDE.

In the case of West Africa, a similar story unfolds with respect to CEAO/UEMOA. CEAO was founded in 1973 on the basis of the cooperation experience gained through UMOA (the monetary union), created in 1962, and UDEAO, which was established in 1966. Part of the region currently covered by the PTA/COMESA, established in 1982, had an earlier history of regional cooperation. It was preceded by the Kenya-Uganda customs union created in 1917 and joined by Tanganyika in 1927; the East African Community was established by these three countries in 1967.

In essence, therefore, only ECOWAS (established in 1975) and SADCC/SADC (created in 1980) can be viewed as regional integration schemes emanating entirely from a post-independence African vision and without a colonial antecedent. A generous interpretation of this finding would probably include PTA/COMESA in this list, but three of the key members of this organization brought to the PTA a rich experience of previous cooperation, even if that experience was partially negative in the sense that the EAC collapsed almost a decade before the birth of the PTA.

Many of these regional integration schemes have evolved from their original manifestations. For instance, CEAO was abolished when UEMOA was created in 1994 as a vehicle for combining the market integration mandate of CEAO with the monetary integration focus of UMOA. Similarly, SADCC became SADC in 1992, while the PTA transformed itself into COMESA in 1993. UDEAC remains basically a market integration scheme that is paralleled on the monetary side by BEAC. It was expected to fold into the larger CEAC, which was established in 1983 in pursuance of the UNECA-LPA vision and grand design of regional integration in Africa. But CEAC has not become operational for lack of funding. Although its treaty was substantially revised in 1992, ECOWAS remains virtually unchanged since its establishment.

SACU also remains largely unchanged, although a vigorous renegotiation discussion has been going on since the early 1980s. More definite movements have occurred on the monetary side, however. In particular, the formalization of monetary integration within the SACU area started in 1974 with an agreement between South Africa, Lesotho and Swaziland to create the Rand Monetary Area (RMA). In 1986, the RMA was transformed into the Common Monetary Area (CMA) and in 1992 independent Namibia was admitted into the CMA. At this point SACU and CMA taken together represent a combination of customs union with monetary integration and convertible currencies.

Measured in terms of degree of integration, it seems clear that CEAO/UEMOA and SACU/CMA, which combine market and monetary integration, are at the top of the ladder. It is also, perhaps, not an accident that both of these schemes have evolved

from colonial antecedents. But they do differ in certain important respects. SACU/CMA is held together by a dominant partner, i.e., South Africa, while UEMOA is anchored by France. Thus, the UEMOA arrangement continues to reflect its colonial roots and may be viewed as a prelude to a full-fledged North-South scheme in the shape of NAFTA.

## ***Motivation and objectives***

Virtually all the regional integration schemes covered by this project express, as their primary motivation, the desire to assist in raising the standard of living of their population. Similarly, they all assume that the way to achieve this overriding objective is to promote greater cooperation and more balanced development of their member states. Compared to the others, SADCC initially had a more specific *raison d'être*, i.e., to reduce the dependence of its member states on South Africa at a time when the latter's regime was politically unacceptable. The specific objectives of most of the regional integration schemes include the elimination of tariffs and other restrictions on trade between members, establishment of a common external tariff against non-members, abolition of obstacles against the movement of persons, services and capital within the integrated area, and harmonization of economic policies among member states. Since they also favour balanced development of member states, most of the schemes include instruments for promoting the growth of the less developed members and for compensating particular member states where necessary.

The schemes differ significantly with respect to their chosen instruments for dealing with the objective of balanced development and compensation.

At least one scheme (SACU) relies solely or primarily on a revenue-sharing formula. A few others, such as PTA/COMESA and SADC, depend on regional projects and regional policies for promoting equitable and balanced development within the integrated area. A third set of regional integration schemes, which contains CEAO/UEMOA, ECOWAS and UDEAC, combines an explicit compensation fund with the allocation of regional projects for the same purpose. In spite of the differences of opinion between South Africa and its partners in SACU, this scheme's compensation arrangement works better than those of other regional integration schemes in Africa. This may have something to do with the way the various compensation funds are financed. SACU has a fairly straightforward revenue sharing arrangement; what is shared according to an agreed formula is a pooled customs tariff revenue. Many of the other regional integration schemes have explicit compensation funds that are financed by contributions from members. They work less well primarily because the required contributions are often not paid when due.



## ***Characteristics of integrating areas***

The initial conditions in some regional integration schemes were more conducive to higher intra-group trade flows than those in others. CEAU/UEMOA may be singled out in this respect. The seven countries constituting this scheme had some complementary structures; inter-sectoral division of labour was important in trade between Burkina Faso and Mali (agricultural exporters) and Côte d'Ivoire and Senegal (relatively industrialized members). Rail links exist between many of the member states; hence, natural barriers to trade such as prohibitive transport costs are lower than elsewhere in Africa. In addition, a high degree of factor mobility prevailed between CEAU countries, against the background of a common currency and French language. Finally, there exists the Conseil de l'Entente, which uses funds from donors and richer members to finance development projects in less developed countries; the need to retain access to these external funds promoted loyalty to CEAU.

SACU exhibits some of these advantages as well. It is, however, a partnership between one relatively large economy and four tiny economies. South Africa accounts for 46% of SACU's geographic area, 87% of its population and 93% of its GDP, and has a significantly larger and more developed industrial sector than the other countries. SACU derives part of its resilience from the long history of significant intra-group trade. In more specific terms, most SACU imports are sourced from or through South Africa. The other members of SACU account for 25% of South Africa's manufactured exports and 10% of its total exports. This level of intra-group trade is, no doubt, facilitated by the relatively low transport costs within SACU, the high factor mobility, the existence of a common language and significant monetary integration.

UDEAC, whose six members also belong to the franc zone, has the advantage of free capital mobility. But labour mobility is severely restricted and intra-group trade is limited. The original nine members of SADC have broadly similar production and trade structures and, in addition, lack the advantages of good transport links and a common currency (or even convertible currencies). Its recent transformation into SADC and the addition of Namibia, South Africa and Mauritius as members should bring about greater complementarities in the economic structure.

Compared to the smaller and more compact schemes referred to above, ECOWAS (with 16 members) and PTA/COMESA (with 22 members) lack many of the initial conditions regarded as conducive to effective regional integration. Both regional bodies exhibit immense discrepancies in market size, production and trade. The dominance of ECOWAS by Nigeria is not accompanied with the same economic linkages associated with South Africa's dominance of SACU (and probably of SADC also). Language, cultural differences and poor transportation and communication infrastructures that hinder intra-group trade in ECOWAS are probably just as potent in the case of PTA/COMESA. Unlike ECOWAS, however, PTA/COMESA visa requirements continue to severely restrict labour mobility.

## **Key integration instruments**

Significant regional integration instruments have been developed in only three of the six schemes examined in this project. These three are CEAO/UEMOA, UDEAC and SACU. In CEAO, the key regional integration instrument is the regional cooperation tax (TCR). This is a special preferential regime with two different objectives. First, it limits intra-regional competition by favouring products from poorer member states over those from more advanced countries. Second, it promotes regional import substitution through explicit discrimination against third-country sources. TCR replaces all duties and taxes levied on imports of member states and thus serves as a common external tariff. But it has an inherent defect. By helping to maintain inefficient industries in the poorer countries and protecting all regional products from outside competition, the TCR contributes to further erosion of the international competitiveness of the integrated area.

Two key instruments were developed in UDEAC, the common external tariff (CET) and the single tax (*taxe unique* or TU). The CET replaced import duties on imports from outside the region. It included a complementary component meant to temporarily compensate member countries for lost revenue due to the harmonization of customs duties. Because of large initial divergences in individual rates, the complementary component of CET varied quite widely among countries; hence CET resulted in differential protection.

The single tax (or TU) intended foster regional industrial production and trade by reducing domestic and import taxes on regional goods relative to extra-regional goods. In effect, the TU replaced all domestic indirect taxes and import duties for industrial goods produced and sold within UDEAC by registered firms. Although TU rates were significantly lower than the CET, the TU was a very discriminatory regime. TU rates varied from firm to firm, by product and by country primarily because each member country determined the rate that applied in its territory.

SACU's key integration instrument is a revenue-sharing formula. All customs, excise and sales duties as well as import surcharges collected in the member states are pooled at the South African Reserve Bank. The formula provides the basis for calculating the amount due to the individual member states—Botswana, Lesotho, Namibia and Swaziland. Because these small countries are in a customs union with a more developed South Africa, the revenue-sharing formula serves as a mechanism to compensate for the negative impact of possible trade-diversion, the loss of fiscal sovereignty and the likely concentration of industrial development in these countries.

## **Constraints**

Virtually all of the regional integration schemes suffer from one design defect or another. In many cases consensual decision-making arrangements, lack of regional level monitoring of the implementation of decisions and lack of power by the regional

secretariat to take initiatives have rendered the schemes impotent. In UDEAC, for instance, the treaty does not transfer sovereignty over any significant matters to the regional authority. As a result, regional integration in trade matters is held hostage by specific national interests. In monetary matters, however, the majority decision arrangement in the franc zone central bank keeps monetary integration on track.

In both ECOWAS and PTA/COMESA, the domestic policy stance has been generally at variance with the ideals of regional integration. Recent reforms moving many African countries away from import-substitution policies and towards greater outward orientation may re-align domestic policies with requirements of regional integration. But the implementation of unilateral trade liberalization programmes, at different speeds and without regional coordination, implies that the undesirable policy variance may continue to be problematic.

Given the relatively heavy dependence of many African countries on international trade taxes, the absence of effective compensation arrangements in many of the regional integration schemes has hindered implementation of certain trade liberalization measures at the regional level. In other cases, attempts to finance compensation funds from contributions have generally been less than satisfactory.

In several key cases, overlapping memberships have created special problems. In West Africa, the rivalry between ECOWAS and CEAO/UEMOA renders both institutions less effective than they could be, partly due to lack of commitment resulting from divided loyalty. More significantly, however, there is a great conflict in the approaches of the two overlapping institutions. On the one hand, CEAO/UEMOA through its linkage with France could, in principle, develop into a North-South regional integration scheme if France were replaced by the European Union. On the other hand, ECOWAS views itself as the West African building block for the ultimate all-African regional integration scheme (AEC). This sharp difference in approach and ultimate destination has created tremendous tensions in both organizations.

In the east and south of Africa, a similar rivalry has emerged—in this case between SADC and PTA/COMESA, another set of two institutions with overlapping memberships. Several scenarios appear to exist for resolving this issue. A merger between SADC and COMESA is, apparently, unacceptable to the former, which would rather dismember the latter into northern and southern halves, with the southern half being then equivalent to SADC. This last scenario would not only eliminate overlapping but would also free SADC to move, under the leadership of South Africa, into a North-South linkage with the European Union, thus replicating the dilemma in the west.

### ***Impact of changing conditions***

The changing political and economic conditions in Africa over the last decade or so and the changes occurring in the global environment have significant implications for the regional integration schemes in Africa. Some of these schemes have recently

revised their treaties or in some other way altered their organizational forms and/or activities in response to some of these changes. The economic policy changes of the late 1980s, particularly those associated with structural adjustment, revealed discrepancies and distortions and pointed out the need to integrate the trade-promoting aspects of CEAO with the monetary harmonization mandate of UMOA. This resulted in UEMOA. The explicitly stated role of France as the guarantor of UEMOA and ongoing changes in the global environment could further transform UEMOA in a possible direct link with the European Union.

In the context of ECOWAS and PTA/COMESA, what the changes associated with structural adjustment have brought about is a realization that unilateral trade liberalization and reduction in the extent of currency over-valuation can have a greater impact on intra-group trade expansion than all the regional protocols that have been signed. However, the uncoordinated nature of unilateral liberalization could mean that the full potential of these changes is not realized in the regional context. The lack of coordination at the regional level also implies that neither ECOWAS nor PTA/COMESA is in a position to monitor and enforce the commitment of member states to their liberalization policies and thus help to strengthen their credibility.

Recent political changes in South Africa radically affected SADCC—transforming it into SADC. These changes rendered redundant SADCC's original reason for existing, i.e., to reduce dependence on South Africa. The new SADC has now welcomed Namibia, Mauritius and South Africa into its fold, and has also become much less inclined to associate with PTA/COMESA. Viewed from the perspectives of South Africa's recent offer to GATT/WTO and its ongoing negotiations with the European Commission, it may be that a South Africa-led SADC could establish a viable South-North link with the European Union, using a more direct route than that presumed in the French-anchored UEMOA.

## ***Performance***

The changes alluded to above are clearly too recent to have significantly affected the historical performance of African regional integration schemes. While they and their implications are clearly important, an evaluation of how and the extent to which they boost or hinder the performance of the various schemes cannot be carried out at this time. What is offered below, therefore, abstracts from the recent changes.

The literature generally suggests, and the results of this project unanimously confirm, that the regional integration schemes in Africa have not significantly increased intra-regional trade. In most cases, results from studies based on gravity models suggest that African intra-group trade is not necessarily low because of factors that work differentially against it, but rather that it is naturally low. Analysis based on comparison of trade ratios over time also shows that in virtually all the integrating regions such ratios have actually declined or remained stagnant over time.

In particular cases, however, the findings of this project suggest specific factors that could help explain this general pattern. In the cases of both CEAO and UDEAC, it seems clear that the chosen integration instruments were virtually guaranteed to discourage rather than promote intra-regional trade. With respect to ECOWAS and the PTA/COMESA, non-compliance with or delayed implementation of agreed liberalization schedules obviously did not enhance intra-group trade expansion.

It is by and large taken for granted that South Africa derives significant benefits from SACU. Clearly, in the absence of this customs union, some of South Africa's exports to its partners in SACU would face severe competition and be lost to suppliers from elsewhere, since South Africa is not necessarily the cheapest source for all the imports of its SACU partners. But for these partners also, it is clear that SACU membership has not prevented them from achieving impressive rates of economic growth or from successfully transforming the sectoral composition of their GDP. Furthermore, in terms of per capita income growth, each of these partners has improved its position relative to South Africa over the past 20 years. Membership in SACU and the duty-free access to the larger South African market that this guarantees has continued to be a major promotional point for the SACU member countries in attempting to attract foreign investment into their economies. Recent surveys of the private sector in these countries also confirm that SACU has been mutually beneficial.

## **5. Trade liberalization experience**

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The case study framework used in this project focuses on a set of common issues. In particular, questions were asked about whether trade liberalization took place. If it did, each case study then went further to determine when and over what period; it also examined the key features of each trade liberalization episode. In addition, the impetus for and the mechanisms of the various liberalization episodes were analysed. The credibility and sustainability of trade liberalization episodes constitute another major issue of concern addressed in the case studies. Finally, an analysis of the short-run and long-run consequences of the trade liberalization episodes was undertaken in each case study.

### ***Pre-liberalization trade regimes***

What were the dominant features of the restrictive trade regimes subjected to change in the liberalization episodes? An understanding of these should provide the background against which the impetus for reform as well as the pressures behind the frequent reversals of policy reform measures can be properly appreciated.

Between the early 1960s and the early 1980s, many African countries built up highly interventionist and protectionist trade regimes. These regimes were broadly characterized, on the import side, by restrictive licensing systems, high tariffs, escalated or cascading tariff structures made up of several layers, varying degrees of import prohibitions, and tight foreign exchange controls. On the export side, the trade regimes feature substantial implicit and explicit taxes as well as frequent use of non-tariff barriers, such as the prohibition of certain export items. These heavily protectionist trade regimes were motivated by several different concerns, some of which were conflicting. This probably accounts for the rather haphazard, incoherent and internally inconsistent nature of the trade regimes that eventually evolved. The implications for the pre-liberalization trade regimes are broadly reflected in the case studies covered by this project.

One of the key problems trade policy had to address in most of the case study countries was government revenue. Given the heavy reliance on tariffs for revenue it is not surprising that fiscal concern was a major motive for imposing high import and, in some cases, export tariffs. At the same time, many of these countries were

highly susceptible to balance-of-payments pressures, given their strong commitments to the maintenance of often unrealistic fixed exchange rate systems. In this context, trade policy often became a substitute for more appropriate policies needed to maintain macroeconomic discipline (such as exchange rate and fiscal policies, for example). Hence, non-tariff import control measures were often applied whenever it became necessary to deal with recurring balance-of-payments crises.

Some aspects of the pre-liberalization trade regimes could also be traced to the desire to protect domestic industries in the context of the import-substitution industrialization (ISI) strategy popular in Africa during the 1960s and 1970s. Evidence to support this includes extensive exemptions from tariff duties and low tariff rates on imported inputs used by local producers. The generally escalated structure of tariffs that imposed high rates on finished products and much lower rates on raw materials provides additional evidence in this regard.

It is important to bear in mind that high tariff rates were also applied to so-called “luxury” goods. These were import items thought to be consumed largely by the rich and were often goods for which no local production facility existed to be protected. Thus, high tariffs did not always reflect the desire to protect local industry; in certain cases they were aimed at raising revenue based on the perceived ability of certain categories of consumers to pay. The pre-liberalization trade regimes of many African countries exhibited a strong relationship between the use of import restrictions and the appearance of balance-of-payments problems. Balance-of-payments concerns, together with budgetary needs, probably had much stronger impact on the evolution and structure of pre-liberalization trade regimes in the case study countries than did the desire to protect local manufacturing activities.

### ***Impetus for trade liberalization***

This study shows that trade liberalization episodes in the case study countries have been brought about by various types of stimuli. A two-way classification of these stimuli helps identify unilateral and multilateral mechanisms. The unilateral liberalization attempts, in turn, consist of several categories. In some cases they derive from conditions imposed on the liberalizing countries for gaining access to external finance in exchange for policy reform in the context of structural adjustment programmes. In addition, some unilateral trade liberalization efforts have either been associated with positive external shocks that enabled some countries to finance their liberalization attempts or related to “own initiatives” that reflected internal policy dynamics and the design and use of innovative schemes to finance the liberalization process.

The multilateral mechanism for trade liberalization in the case study countries refers, essentially, to those liberalization efforts that were designed and implemented in the context of specific regional integration schemes. This study offers a unique

opportunity to determine the existence of this trade liberalization mechanism, and to evaluate its significance and effectiveness particularly in relation to the experiences of Côte d'Ivoire, Ghana and Nigeria within ECOWAS; those of Mauritius, Kenya, Tanzania, Uganda, Zambia and Zimbabwe within the PTA/COMESA; and that of South Africa within SACU.

Among the four different types of stimuli for trade liberalization identified above, the most prevalent in the case study countries was the liberalization process embedded in the structural adjustment programmes. These programmes shaped the design, scope and sequence of trade liberalization processes in nine of the ten case study countries since the mid 1980s; the single exception is South Africa. Five of the nine countries, i.e., Côte d'Ivoire, Kenya, Tanzania, Uganda, Zambia and Zimbabwe, experienced partial reversals of their trade liberalization processes. Nigeria partially reversed in 1988 and virtually abandoned its process in 1994. Only Ghana and Mauritius appear to have pursued their programmes persistently.

Positive external shocks stimulated some trade liberalization episodes in several case study countries. Liberalization episodes associated with this stimulus were typically temporary and partial, usually characterized by temporary and limited relaxation of import restrictions and exchange controls. In the cases of Kenya and Tanzania this type of liberalization occurred in response to the commodity booms of 1976/77. The episodes were short-lived; the collapse of 1979/80 generated policy reversals and brought in even more severe import restrictions and exchange controls than before. The Nigerian trade liberalization episode of 1970-1976 had a similar origin in the positive external shock generated by the oil export boom, and it suffered a similar fate as soon as the external shock was reversed.

Several varieties of the "own initiative" stimulus for trade liberalization explain a number of trade liberalization episodes in some of the case study countries. In South Africa, internal policy discussions led, in 1972, to initiatives that focused on the reduction of the anti-export bias inherent in the existing ISI development strategy. Subsequent policy reviews between 1983 and 1993 led to a new industrial strategy featuring a more neutral trade regime with tariffication of quantitative restrictions and a simpler, more transparent tariff structure.

Mauritius began reducing the anti-export bias inherent in its ISI strategy between 1970 and 1979, largely as a prelude to more comprehensive trade liberalization associated with its structural adjustment programme in the early 1980s. Compared with several of the case study countries that made a similar attempt, the sheer scale and effectiveness of the effort in Mauritius set it apart from the others.

Another variety of "own initiative" stimulus for trade liberalization is based on the Own Funded Import Schemes. Under these schemes, importers were allowed to bring in goods without official foreign exchange allocation to finance such imports and with no questions asked about the source of financing. The schemes were aimed essentially at ameliorating generalized shortages of essential goods and controlling



inflation. These schemes were used to support some trade liberalization episodes in Zambia, as well as in Tanzania during 1984-1986 and Ghana in 1967-1972.

The least significant stimulus for trade liberalization among the case study countries is membership in a regional integration arrangement. The trade liberalization scheme of ECOWAS remains largely unimplemented. It has, in fact, been virtually ignored as Côte d'Ivoire, Ghana and Nigeria have concentrated policy and implementation attention on the unilateral trade liberalization processes contained in their individual structural adjustment programmes. Designed and implemented at national levels, these programmes uniformly ignored the regional dimensions of unilateral liberalization and paid no attention to the regional integration obligations of particular countries. With regard to the PTA/COMESA, it seems clear that pursuit of more intense unilateral liberalization at each member country level has overshadowed the preferential trade liberalization scheme. In any case, trade liberalization has progressed much faster under the unilateral mechanism.

The most dominant among the stimuli for trade liberalization noted in the case studies are linked to conditions imposed by structural adjustment programmes—they appear in more than 80% of the liberalization episodes identified by the policy accounts. In addition, these trade liberalization episodes have also been the longest sustained and the most comprehensive among the liberalization attempts identified and analysed in this study.

### ***Scope and extent of trade liberalization***

In terms of scope, trade liberalization processes covered tariffs and non-tariff measures such as quantitative import restrictions and exchange control.

Tariff structures in all case study countries were substantially compressed by reducing the number of tariff categories. Both Tanzania and Zambia brought the large number of their tariff categories to 3. Kenya reduced its own from 25 to 6, while Côte d'Ivoire moved from 10 to 6. Mauritius reduced the number of its tariff categories from 60 to 10. Nigeria's tariff rationalization and restructuring process was pursued during 1986/87. South Africa's efforts in this direction started only in 1995. In virtually all case study countries, the process of compressing tariff structures has been gradual, but has generally intensified in each country across trade liberalization episodes. As a consequence of this compression process, the rates of protection offered to industries in each country is become much less varied, the scope for discretionary or ad hoc granting of protection to specific activities is considerably reduced, and the transparency of tariff policy is enhanced.

Tariff structures were not only compressed in all case study countries, tariff rates were also substantially reduced. In Mauritius, the maximum tariff rate was reduced from 250% to 100%; Tanzania's maximum rate fell from 200% to 50%; Zambia reduced its own from 150% to 50%; and the maximum rate in Kenya was reduced

from 170% to 40%. Reflecting both tariff structure compression and rate reductions, tariff rates in Ghana now range between 100% and 40%, while those in Zimbabwe are between 5% and 30%.

Overall, lower tariff rates have generally not reduced total tariff revenue, as had been feared. In most cases, revenues increased as a result of increased compliance by taxpayers due to the reduced rates. Moreover, increased imports generated by external assistance considerably boosted the tax base in some countries while the steep rise in the local value of imports, brought about by large devaluations, generated a similar result in other countries.

Dramatic changes also took place with respect to quantitative restrictions, which were eliminated in several cases and either partly or completely converted to tariffs in others. Ghana abolished its import licensing system in 1989 and Mauritius eliminated its import permits in 1991. Zambia followed suit in 1992, with Kenya and Tanzania achieving the same result a year later. By 1990, South Africa had reduced its quantitative restrictions by 85%. The remaining countries also significantly reduced the proportion of their imports covered by restrictions. The typical mechanism for achieving these reductions was a switch from a positive list of permitted imports to a small and progressively reducing negative list of prohibited terms.

The process of reducing quantitative restrictions was helped along by the elimination or relaxation of foreign exchange controls in many of the countries. A good indicator of this policy change is the sharp decline in the parallel market premium for foreign exchange. This decline partly reflects the extent to which the demand for foreign exchange (to purchase imports among other uses) is less restricted by controls. Exchange rate premiums were virtually eliminated in Ghana, Kenya, Mauritius, Uganda, Tanzania and Zambia. In these countries, current account transactions are free of restrictions and determination of currency rates is market based.

The effectiveness of the liberalization of tariff and non-tariff measures is broadly reflected in the trend of effective rates of protection. Typically, these rates fall with trade liberalization. Consistent with this expectation, significant rationalization and reduction in effective rates of protection were achieved in nearly all the case study countries. Nigeria is the only country in which the general downward trend in effective rates of protection was reversed. Starting from a pre-reform level of 33%, Nigeria's average effective rate of protection fell to 23% during 1986/87, only to rebound to 41% in 1991.

To sum up, it is clear that both tariff and non-tariff measures were significantly liberalized in the ten case study countries. The more liberal use of exchange rate changes for clearing disequilibrium in the foreign exchange market considerably reduced the traditional reliance on trade policy instruments for managing balance-of-payments pressures.

## ***Credibility and policy reversals***

African trade liberalization attempts suffer from problems of credibility and sustainability, which are typically reflected by reversals of trade liberalization initiatives—as amply demonstrated by the varying experiences of the ten case study countries. Mauritius and Uganda are the only two countries in this sample that did not reverse policy. Two countries experienced total policy reversal: Zambia after the collapse of its foreign exchange auction in 1986 and Nigeria in 1994. Several countries experienced fairly frequent partial policy reversals. Kenya has had at least seven liberalization episodes since the early 1970s, most of which were separated by partial reversals. Similarly, Ghana experienced five shifts in trade policy over a period of about 15 years. Obviously, frequent and sharp policy changes undermine the credibility of subsequent liberalization attempts.

Mauritius appears to be the most successful of the ten countries in achieving credibility. Its first liberalization episode of 1979-1985 focused primarily on stabilization and exchange rate adjustment with very little change in direct trade policy measures. Comprehensive trade policy adjustment followed during the second liberalization episode of 1991-1994. It appears that Mauritius established credibility by first demonstrating its determination in the context of a traditional stabilization programme that included large devaluations in 1979 (23%) and 1981 (17%).

By contrast, many trade liberalization attempts were too closely associated with the prevailing control regime, which, unlike Mauritius, had not built up a reputation for credible reform in other policy areas.

Most policy reversals revealed in the case studies were triggered by balance-of-payments and fiscal incompatibility. The reluctance of governments to refrain from using traditional trade policy instruments for addressing incompatibility issues made policy reversals virtually unavoidable. Exchange rate adjustments appear crucial in this respect. Most of the successful trade liberalization episodes were accompanied by large devaluations, while many of the policy reversals can be traced to the reluctance to make sufficient and determined use of exchange rate adjustment. It seems to be the case that in African economies where there is a historical aversion to changing the exchange rate, large devaluations can serve as powerful signals of government's determination, which could, in turn, enhance policy credibility.

## ***The impact of trade liberalization***

The assessment of the impact of trade liberalization was carried out against several broad expectations drawn from received wisdom. First, trade liberalization provides expanded market opportunities; when coupled with reduced discrimination against exports, these allow exploitation of comparative advantage, permit greater capacity utilization and enhance exploitation of economies of scale. Second, by reducing anti-

export bias trade liberalization stimulates export performance, particularly non-traditional exports. Third, increased competition from abroad and enhanced access to better technology made possible by trade liberalization induce technological innovation and higher productivity. In principle, these impacts of trade liberalization are channelled through various resource allocation and supply responses.

The typical target variables in an evaluation of the impact of trade liberalization include changes in output, in various components of trade, in the performance of the manufacturing sector and in employment. On this basis, Mauritius stands out as the country with the most successful experience with trade liberalization. Its fairly long and effective trade liberalization process had significant positive impacts on trade, output and employment over the 1979-1990 period. Its import/GDP ratio rose by 35% and the export/GDP ratio increased by 46%. Real GDP growth was maintained at an average annual rate of 5.6%, while the unemployment rate declined steadily from 28% in 1982 to less than 5% in the 1990s. It should be noted, of course, that the maintenance of macroeconomic stability, other supportive policies and a favourable external environment for exports played significant roles in achieving these results.

In Uganda, the import/GDP ratio increased from 9% to 20% between 1989 and 1993, but the export/GDP ratio remained roughly constant at 5%. Only massive inflow of resources (from official and private sources) made it possible to sustain the trade liberalization process. Real GDP grew by an annual average of 6.4% between 1991 and 1995 while anecdotal evidence suggests positive impacts in terms of employment and performance of the manufacturing sector. In spite of the increase in the tax revenue/GDP ratio from 7% to 12% between 1991 and 1995, Uganda's liberalization could encounter fiscal incompatibility problems in the near future. In the same way, Uganda's heavy reliance on massive external financing to maintain the payments compatibility of its trade liberalization process should ring alarm bells.

Zimbabwe's trade liberalization process is more difficult to evaluate in terms of its probable impact. This is because the episode is relatively short and largely coincides with a sharp negative drought shock that caused a drop of 7.7% in real GDP in 1992 alone. Overall, however, real GDP growth averaged 3.4% per annum in the early 1990s, while the manufacturing export sector grew by 19% in real terms over the 1990/91 - 1994/95 period. It is also estimated that employment increased by 18.4% between 1991 and 1995.

In spite of frequent but partial policy reversals, Kenya's trade liberalization has had positive effects on growth in imports, exports, output and employment. The import/GDP ratio rose from 26% in 1972 to 36% in 1993, while the export/GDP ratio increased from 26% to 42% over the same period. Real GDP growth averaged 5% per annum in 1988 and 1989, then recorded less than 5% annual growth rate until 1995 when it bounced back to 5%. Trade liberalization does not appear to have had any marked impact on the manufacturing sector, however. A possible threat to the current liberalization process is the reliance on external financing for temporary

balance-of-payments support. This does not appear to have affected the credibility of the liberalization process, however.

In Tanzania, liberalization of the exchange regime rather than trade liberalization has had dominant effect on the growth of imports, exports and output. In South Africa, trade liberalization prior to 1995 focused largely on export promotion measures to eliminate the anti-export bias inherent in the protective trade regime. Import liberalization has only just started. Export promotion measures combined with exchange rate depreciation helped to produce an average annual export growth rate of 7.7% over the 1984-1990 period.

Ghana has had a fairly long period of trade liberalization experience, but the results have been less than impressive. While real GDP growth averaged over 4% per annum from the mid 1980s to the early 1990s, the response of non-traditional exports was modest. Sectoral composition of outputs shifted away from import substituting and non-tradeables to tradeable sectors, as anticipated. But unemployment appears to be worsening due to the de-industrialization consequences of trade liberalization and public sector retrenchment programmes.

The results of the trade liberalization experiences of Nigeria and Zambia have some similarities. In both cases, a dominant mineral sector seems to have deflected the impact of trade liberalization, although in both cases the policy was reversed before it could have any real impact. In any case, trade liberalization measures probably had only a marginal effect on the performance of the Zambian economy. During the decade from 1983, the import/GDP ratio fell from 52% to 33%, while the export/GDP ratio declined from 29% to 20%. In the case of Nigeria, trade liberalization had no significant effect on output, employment or imports.

A few summarizing generalizations can be made on the basis of the trade liberalization experiences of this set of countries. First, there was a shift of resources away from import-substituting and non-tradeable sectors to the tradeables. As a result, exports responded positively, although modestly, and trade shares generally increased. Second, some amount of de-industrialization occurred in some countries. Trade liberalization unleashed competitive pressure that many previously sheltered and inefficient industrial firms have been unable to cope with, but new export-oriented activities have not bloomed sufficiently to take up the slack. Finally, continued credibility of some of the trade liberalization processes faces serious challenge as their heavy reliance on external financing may not be sustainable.

## **6. Opening up and linking Africa together**

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African regional integration schemes have typically been based on trade creation and trade expansion objectives, even though they have also been driven by other non-economic concerns. This primary trade policy focus of regional integration schemes suggests that regional integration and trade liberalization processes could be closely associated. This AERC collaborative project took off from this premise.

In general, trade liberalization can be viewed as one of the means through which the primary objective of regional integration schemes, i.e., trade expansion, can be achieved; regional integration may be thought of as one of the mechanisms for implementing a regionally coordinated trade liberalization programme. This section addresses both of these perspectives.

### ***Opening up Africa through trade liberalization***

Mainstream literature on trade and development suggests that trade liberalization that produces a neutral or outward oriented trade regime confers certain productivity-enhancing and growth-promoting features on the liberalized economy. Prominent among these are improvement in the efficiency with which resources are allocated, increase in competition and product specialization, enhanced ability of the economy to attract foreign investment, and creation of a favourable environment for technology transfer. Within an open or outward oriented trade regime, technology can be transferred through several distinct mechanisms, for example, as an integral part of direct foreign investment. The import of capital goods that embody current technology constitutes another transfer route. In addition, increased competition that induces exporting firms to operate at or close to the frontiers of technological development provides another technology transfer mechanism.

Insights derived from endogenous growth models in which trade plays a role in promoting growth through its function as a mechanism for diffusing technological innovation are broadly consistent with the above. The focus here, however, is on a specific aspect of the mechanism by which the growth promoters are imported. This perspective is particularly relevant for Africa where it would be reasonable to associate the growth-promoting effect of expanding trade primarily with the productivity-

enhancing characteristics of technology embodied in, and the increased capacity utilization permitted by, increased imports of capital and intermediate inputs.

It is clear that both perspectives recognize the significant role of exports in the process. This significance derives not only from the reality that exports can be an important vehicle for technology transfer in their own right, but also, and perhaps more importantly, they are the primary source for financing the indispensable bottleneck-breaking and technology-bearing imports.

The evolution of trade regimes of many African countries in the 1960s and 1970s was largely ad hoc, reflecting attempts to use one instrument (i.e., trade policy) to achieve several (sometimes conflicting) objectives. In addition to their use for generating fiscal revenue and confronting balance-of-payments problems, import control measures were often used as instruments of industrial policy. In general, however, the experience of these countries shows that budgetary needs and balance-of-payments concerns had a much stronger impact on the evolution and structure of their trade regimes than did the desire to protect local industry. This experience appears to be broadly consistent with basic principles that suggest the revenue-raising role of import tariffs would dominate industrial protection as long as foreign exchange allocation is the binding constraint on imports. Only with foreign exchange liberalization does the tariff structure become the principal source of protection.

The African trade policy reforms that began in the mid 1980s and are, in many countries, still going on, achieved some significant results. In general, these reforms typically increased the relative price of exportables compared to non-tradeables; they also reduced, to some extent, the anti-export bias within the tradeables sector. Much still remains to be done, however, especially in terms of rationalizing the trade regime.

Recent liberalization efforts have generally concentrated on the import side and have, to that extent, not paid sufficient attention to the elimination of the anti-export bias inherent in the trade regime. In particular, little progress has been made in establishing efficient mechanisms for giving exporters access to inputs at internationally competitive prices.

Future trade policy initiatives in Africa should obviously derive from the region's long-term development strategy, which, in consonance with experience in other regions, should stress broad outward orientation. An outward oriented development strategy presumes that aggregate economic growth will be export-led in an environment in which macroeconomic balance and stability are maintained. In the peculiar circumstances of Africa, with its rudimentary industrial sectors, several important elements of an outward oriented development strategy should be integrated. First, the existing manufacturing sector needs to be restructured since its current structure and efficiency levels (built up under more interventionist trade and exchange rate regimes) are ill-suited to exporting. Second, the existing incentive regime should be altered to provide exporters with access to inputs at internationally competitive prices, net of tariffs and indirect taxes. Third, appropriate proactive measures should

be used to assist manufacturers and exporters to cope with the rigorous production and learning-by-doing requirements of international markets and the difficulties of gaining access to the information and technology necessary for effective competition in those markets.

Industrialization is clearly an important component of sustainable overall economic development; and the experience of other rapidly developing countries and regions suggests that the export of manufactured goods is one of the key elements of the dynamism and impressive economic growth performance of these countries and regions. Similarly, African countries should be justifiably concerned about the survival and future development of an efficient and export-oriented manufacturing sector as an important component of their long-term development. This concern translates, in trade policy discussions, into the idea that some degree of protection is necessary as part of the proactive measures aimed at encouraging the expansion of the region's manufacturing sector. In other words, there exists a case for some non-zero import tariff levels and a non-uniform import tariff structure in African countries not just for revenue-raising purposes but more explicitly to protect local manufacturing activities from foreign competition.

At the same time, however, considerations of allocative efficiency suggest several qualifications. First, the level of import protection should be moderate (perhaps no more than 25%) to limit the relative price distortions they can create and hence the damage they can do to the economy. Second, import protection should be strictly limited, time bound and related to some clearly understood and measurable performance standard. Third, the tariff structure should be fairly simple, reflecting a limited number of tariff rates to ensure greater transparency.

As indicated earlier, in relation to the export sector, trade liberalization should include policy changes that produce an outward oriented trade regime that explicitly favours and actively promotes exports. This reflects the reality, based on accumulated experience of other developing regions, that good export performance is not just a desirable goal in its own right but is also a critical means to other important ends, i.e., deeper import liberalization and more robust overall economic growth. Exports are, essentially, a means of acquiring the foreign exchange with which to purchase the increased imports made available through trade liberalization. Therefore, good export performance plays a pivotal role in sustaining import liberalization to the extent that increased flow of foreign exchange resulting from expanded exports helps to reduce the need for import compression.

The elimination of disincentives against exporters including regulatory requirements is generally not likely to pose serious fiscal problems in the trade liberalization process. Therefore, there is a strong case for focusing immediate policy attention on encouraging exports, while leaving major import liberalization attempts until later, when sufficient export response can provide the financing for further import liberalization. In other words, whenever export performance can be more readily



induced through specific export promotion measures, it would be reasonable to implement them before deeper import liberalization is attempted. A successful and sustainable import liberalization programme requires successful exports.

The speed at which the rationalization of the tariff structure and the lowering of tariff rates should be achieved would obviously depend on each country's initial conditions, the response of its export sector and its access to external financing. Rapid and deep trade liberalizations may generate unsustainable import surges. Such sharp import increases can, of course, be financed by either a comfortable and steady flow of foreign exchange earnings and stock of reserves or through an adequate and sustained level of foreign assistance. Countries that cannot count on an assured, adequate and sustainable flow of import financing must necessarily be more circumspect with regard to both the speed of tariff reduction and the ultimate target tariff range envisaged in their trade liberalization programmes.

Prior achievement and continuous maintenance of macroeconomic balance and stability are essential for reaping the benefits of import liberalization. Similarly, a more flexible and responsive exchange rate policy backed with adequate financing is necessary if generalized import liberalization is to be consistent with the maintenance of balance of payments stability. When these pre-requisites have been satisfied, standard trade policy instruments can be released from inappropriate revenue-raising and balance of payments objectives so that they can focus explicitly on the more legitimate role of enhancing efficiency of resource allocation and promoting long-term development via industrialization, export expansion and diversification.

The context in which trade liberalization programmes are implemented has significant implications for their sustainability and success. Several key features characterize most of the recent trade liberalization episodes in Africa in this respect. First, these were unilateral trade liberalization attempts that focused primarily on imports. Second, they were designed and implemented as integral parts of structural adjustment reform packages. Third, they were induced by external financing. Fourth, they ignored regional spillovers and adverse consequences of lack of regional coordination and harmonization. Many of the aid-induced trade liberalization attempts have been incompatible with underlying fiscal and balance-of-payments realities in the absence of external financing.

The credibility of many trade liberalization episodes has been suspect, while quite a few have suffered reversals. It seems that their aid-induced nature and their inherent incompatibility with basic economic reality in the absence of assured long-term external financing gave private economic agents sufficient reason to doubt their credibility and sustainability, which, in turn, led to ineffective and anaemic response.

While unilateral and aid-induced trade liberalization may be inherently prone to credibility and sustainability problems, it may well be that these problems can be ameliorated if trade liberalization attempts are designed and implemented in the context of some regional or multilateral agreements or, in the case of unilateral efforts,

if the results are registered with and embedded in an international agreement. The former case has several desirable features. For one, peer pressure and reciprocity may enable each country to take liberalized policy actions that they would otherwise hesitate to take unilaterally. Moreover, such policy measures become less susceptible to pressures from local anti-reform interest groups in each country. The fear of group penalty helps all the participating countries lock in the achievements of liberalization by rendering each country's policy reform largely irreversible. In this sense, credibility of trade liberalization is invariably enhanced in the context of the "reciprocal-threat" arrangement in which the certain reactions of partners make unilateral policy reversal too costly to contemplate.

Based on the observations that there has been little or no trade liberalization in Africa implemented in the context of regional integration schemes with strong and effective "reciprocal-threat" features, and that donor-supported unilateral trade liberalization attempts often lack credibility and are highly susceptible to reversal, a couple of options are worth exploring in the future. Clearly, the credibility of African trade liberalization attempts would be enhanced if the resulting tariff ceilings were "bound" under the provisions of the GATT/WTO agreements. This would be the easier option to implement since virtually all African countries are already (or can become) parties to these agreements. A second option would be for future African trade liberalization measures to be implemented, not unilaterally as hitherto, but in the context of an effective North-South regional integration arrangement with strong built-in "reciprocal-threat" features that could serve as sufficient deterrent to policy reversal. Since such an arrangement does not yet exist and its costs and benefits to all potential participants are currently unknown, it remains to be seen whether it would in fact dominate the former as a viable policy option.

### ***Linking Africa together via regional integration***

The need to link African countries together is, to many in Africa, virtually self-evident. The small size of the typical African economy and the resultant constraints on rapid economic development, the growth-retarding nature of the hub-and-spoke production and trade pattern inherited from Africa's colonial past, and the desire to channel the neighbourhood effects and regional spill-overs into more positive growth-enhancing directions constitute rational and basically economic reasons for seeking closer cooperation among African countries. This search is also motivated by non-economic reasons. Pan-Africanism, as an expression of continental identity, unity and coherence, constitutes the essentially political bedrock of regional integration in Africa. This political inspiration seeks to create a strong African bloc that could be used effectively in the international political arena, for dealing with security concerns and for use as a vehicle for the resolution of regional conflicts in Africa.

The combination of economic and political rationale for the existence of various regional integration schemes in Africa may provide part of the explanation for why the existing regional integration arrangements have failed to fulfill the high expectations attached to them as vehicles for improving the economic performance and welfare of Africa. In the ultimate, of course, and as the treaties and protocols of most of the African regional integration schemes clearly demonstrate, regional integration remains essentially an exercise in economic relations between countries. Hence, any regional integration scheme must, in the end, be justified in economic terms.

The basic economic rationale and goal of African regional integration can be broadly described as follows. Given the small size of the economies, pulling them together can be a useful means of first increasing intra-regional trade and then promoting economic development through industrial growth. In this framework, trade expansion occurs largely through import substitution within the regional market. In essence, therefore, each regional integration scheme could be visualized, in its initial phase, as an inward-looking instrument of industrialization and economic growth. Subsequently, however, if the scheme achieved reasonable success in this initial phase, it could shed its inward-looking characteristics and become an instrument for projecting the integrated region more positively into the world market. The infant industries that develop under the regional import substitution framework could first learn to export within the protected regional market, but eventually would become efficient enough and strong enough to face world competition without further protection.

In Africa, this model of regional integration has not lived up to expectations for a number of reasons. First, the individual African economies are so small that even when combined in the various regional integration schemes that have dotted the African landscape over the last 30 years or so, the larger regional markets have still been quite small by international standards and hence not large enough to achieve high levels of industrial growth and efficiency. Secondly, the structure and efficiency levels of industries that grow within these protected regional markets are not generally sufficient to enable them to compete effectively in the world market. Third, these expectations have turned out to be largely hypothetical, in any case, since the creation of integrated regional markets has remained an elusive and distant goal, partly because the regional integration model is probably inappropriate and, perhaps more significantly, because the various integration schemes have not been seriously implemented.

Despite the widely documented failures of African regional integration schemes in the past and clear indications of current uncertainties, the idea of regional integration continues to be popular, while enthusiasm for it is high and actually appears to be rising. Regionalism is an ideal that is apparently here to stay. Many still believe that the establishment of larger political and economic units in Africa would enhance the

process of development. These larger units may not necessarily be concerned primarily with preferential trade arrangements but more broadly with cooperation on many economic issues. In effect, a constructive approach in charting a path into the future would be to devise suitable integration mechanisms that would exploit the apparent commitment to the ideal of closer collaboration in Africa and, at the same time, ensure that the resulting regional integration arrangements contain strong outward oriented features.

One such mechanism would pull back somewhat from the rather high level of economic integration envisaged in the treaties and protocols of the existing regional integration arrangements, including the proposed African Economic Community. Under this mechanism, current integration schemes would give way to functional and thematic regional cooperation arrangements between various countries to implement joint infrastructure projects in such areas as transport and communication, development and management of water resources, provision of educational and research facilities, and the establishment of codes on cross-border investment and the movement of persons. It is suggested that this functional and thematic form of regional cooperation has several desirable features.

First, it would facilitate the build-up of critical infrastructures requiring high-cost and indivisible investment, which should generate lower unit costs when provided on a regional rather than national scale. Second, this form of regional cooperation would be more flexible and pragmatic in circumventing problems posed by nationalism and equity regarding the distribution of costs and benefits of integration. Third, it is, in any case, better suited to dealing with the range of physical and technical barriers to intra-regional trade that may lie outside the direct purview of trade policy. Fourth, experience gained in this process as well as the infrastructure developed would lay the foundation for subsequent deeper economic integration and the acceptance of the need to transfer some aspects of national-level sovereignty demanded by closer integration.

This “pull back” approach is probably too defeatist, given the energy and resources that have already gone into designing and implementing regional integration schemes in Africa. A more forward looking approach would perhaps be more acceptable. Such an approach would have to start with the recognition that the “old style” import substitution industrialization model has fallen out of favour and that regionalism based explicitly on outward orientation would be more consistent with the emerging policy environment in Africa. This starting point would be without prejudice to the desire to provide domestic industries an opportunity to learn to cope with competition in the larger regional market before being exposed to the more intense competitive pressures in the world marketplace. But it would view the larger regional market primarily as an entry point into and the conduit through which the international market would eventually be accessed.

The characteristics of regionalism that would capture the basic features articulated above imply that the existing African regional integration schemes should be converted from free trade arrangements into open-ended customs unions. This regional integration model requires that a common external tariff be established and that all national level tariffs come down to the lowest level existing in the union when it is established. The open-ended customs union model has several desirable features. First, the effectiveness of lobbies against liberalization is much more diluted since region-wide lobbying is necessary to block reform, whereas, in a free trade area, tariffs are responsive to national level interest groups.

Second, the open-ended feature of this model facilitates the entry of new members as long as they are prepared to accept the rules and responsibilities of the union. Third, the common external tariff removes the need for rules of origin which often cause conflict and perpetuate protection in schemes based on the free-trade-area model. Fourth, the common external tariff provides the revenue base for an appropriate compensation arrangement in the union; this is an in-built revenue source that is absent in free trade areas and implies that compensation funds must be generated through direct contribution from members.

African regional integration schemes have the potential to contribute to Africa's process of economic development. They suffered in the past, and are probably doing so currently, from design faults and implementation problems. Their potential will not be realized until both of these problem areas are appropriately addressed.

## **7. Linking Africa with the world**

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Regardless of their specific trade policy stance, the economies of African countries have traditionally been heavily influenced by developments in the world economy as these are mediated through changes in commodity prices, changes in the prices of African imports, flows of foreign assistance and direct foreign investment, and, more recently, the external debt overhang. Recent trade liberalization and other policy reforms in Africa could substantially propel Africa into a closer embrace with the world economy.

This section focuses on some of the key features that would be involved in the process of linking Africa with the world. It also considers the role of trade liberalization in the linking process and concludes with a discussion of some of the mechanisms for endowing African trade liberalization attempts with greater credibility and sustainability that also imply and are consistent with greater integration of Africa into the global marketplace.

### ***African trade liberalization in the context of globalization***

The ongoing trade liberalization and related economic policy reforms in Africa can, in some sense, be seen as part of a more general phenomenon among developing countries world-wide. These policy reforms feed, in turn, into an increasing globalization that further links together world economies, both developed and developing. In broad terms, globalization offers important opportunities for accelerating economic growth all over the world. Hence, it is suggested that countries and regions of the world that are unable or unwilling to integrate themselves into this emerging mainstream of the global economy might not benefit from the growth-enhancing features of globalization.

The literature suggests that deeper integration into the world economy matters because it is associated with growth in several ways. First, integration tends to promote higher growth through such channels as improved resource allocation, greater competition, technology transfer and learning, and improved access to foreign capital. Second, trade and investment tend to increase more rapidly in countries that have opened themselves up to the world economy than in those that have not. Third, there is a reverse flow; growth itself tends to promote integration. Fast-growing countries

attract more foreign direct investment and secure better and cheaper access to the world's financial markets, and imports rise faster.

The experience of many developing countries during the 1970s and 1980s appears to be broadly consistent with these expectations. It can be shown, in particular, that during this period, the more open economies grew faster than the closed ones, while structural change corresponding to a shift in reliance from primary production to manufacturing occurred faster in open economies than in the relatively more closed ones. In the aggregate, between 1960 and 1990, the volume of world merchandise trade increased more than five-fold, a growth rate that substantially exceeded the trebling of world merchandise output over the same period. This sharp difference in growth rates reflected growing openness and interdependence of national economies.

African countries are more weakly integrated into the global economy than are countries in other regions of the developing world. For instance, African countries did not participate in the virtually universal trend of increasing trade share over this period; in Africa these shares were lower in 1990 than they were in 1960. The decline in African trade ratios over this period was also accompanied by extremely low ratios of foreign direct investment to GDP and virtual exclusion of African countries from the global financial markets. This reality of the African experience may suggest that both inadequate integration into the world economy and consequent lack of growth have led to the region's marginalization in the world goods and capital markets.

Globalization is clearly not free of problems. It can be linked to greater vulnerability of individual countries to external shocks, which, in turn, tends to negatively affect economic performance. It lacks an effective overall macroeconomic manager, with the rules and institutional arrangements that govern and constrain economic behaviour in the social interest in the typical nation-state remaining largely absent at the global level. In addition, while the essentially free global market economy can generate large inequalities in income distribution between regions, countries and even individuals, it lacks the necessary equity-oriented arrangements for easing these inequalities. It can thus generate potentially severe and world-wide macroeconomic turbulence.

As in other areas of policy making, therefore, greater integration into the global economy is associated with benefits and costs. Globalization does not necessarily offer the same potential opportunities to all countries and the costs may also be differentiated. The terms and conditions under which Africa links itself to the world through trade liberalization and associated policy reforms and in the context of the general trend towards increasing globalization should reflect choices that explicitly recognize the costs and benefits of globalization and assign an important role to risk aversion. More specifically, Africa's long-term development strategy would probably involve the rise of selective and differential incentives and disincentives in guiding a broad range of economic activities. At the same time, the proactive measures necessary for local capacity building may neither permit the establishment of totally level "playing fields" in certain policy areas nor be consistent with total harmonization of

Africa's domestic policies with international standards over which the region may have little influence.

### ***External agencies of restraint and African trade liberalization***

Many African trade liberalization attempts have suffered from lack of credibility and policy reversals. One explanation for this appears to be lack of effective restraints on African governments, which gives room for capricious and frequent changes in trade policy. Thus, in the absence of an effective mechanism for locking in reform, reversal of trade liberalization has become a serious problem in Africa.

Credibility and sustainability are critically important characteristics of effective trade liberalization. If key economic actors do not believe that new incentive structures created by a trade liberalization episode will be sustained, they will not respond in the expected development-oriented manner and the effects of the reform will be blunted or even negated.

The failure of private investment to recover in Africa in spite of considerable policy reform efforts may be important evidence that lack of credibility of these policy reform efforts has been costly. The enormous increase in foreign direct and portfolio investment in developing countries in the 1980s and 1990s has almost completely by-passed Africa. Domestic investment has not filled the gap. The combined result of these trends is the low level of private investment, which probably constitutes the most serious constraint to economic recovery and growth in Africa.

Because lack of credibility and sustainability of trade liberalization negatively affect its effectiveness, it is important to establish appropriate mechanisms for locking in policy reform through effective agencies that can restrain African governments. These governments are not in a position to create viable, effective domestic agencies of restraint, given the fragile nature and absence of widespread confidence in the rule of law in many African countries.

The inability to establish viable domestic agencies of restraint by individual African countries is not necessarily unique. Many countries outside Africa, both developing and developed, have found external commitments useful as something policy makers can hide behind when attempting to ward off local interest groups seeking to curtail reform.

Typically, the need for external restraint has been met by the creation of inter-governmental institutions that work essentially by means of reciprocal threats. In other words, these agencies provide the mechanism by which a government could credibly lock in the achievements of its trade liberalization efforts, with enforcement supplied by the certainty of punishment by the other partners to the agreement. In general, these institutions are not only reciprocal, they also have penalties at their disposal sufficient to deter unacceptable behaviour by any member and an incentive



to invoke these penalties. Their reciprocal nature requires that the governments that choose to be bound by them also participate in the design of the rules and in the supply of enforcement. Reciprocity and full participation by individual members ensure that the agency will not abuse its power to extract behaviour the participating governments do not voluntarily choose.

African countries have, in principle, several options to choose from in selecting an external agency of restraint to assist in enhancing the credibility of their trade liberalization efforts. For instance, each country could use the regional integration scheme to which it belongs as an agency of restraint. However, it appears unlikely that an African regional integration scheme can serve as an effective agency of restraint. The reality of the existing schemes is that the potential penalties they can impose for breaking an agreement are quite small. In any case, they have not demonstrated a clear ability and willingness to impose significant penalties on erring members.

A more viable option for African countries would be to use the GATT/WTO as an agency of restraint. This is, in fact, the premier institution at the global level that monitors and restrains the behaviour of contracting parties or member countries in the trade policy arena. Under the GATT/WTO framework, tariff bindings lock in progress on the domestic front and are useful in warding off local lobbies seeking further protection. These internationally registered bindings then become an important mechanism of importing credibility for a trade reform programme. Although most African countries subscribe to GATT/WTO and could use it as an agency of restraint in support of their trade liberalization efforts, they have not in fact done so. African countries have historically had limited participation in GATT/WTO, including the recently completed Uruguay Round of multilateral negotiations.

Prior to the Uruguay Round, less than half of the African members had lodged their tariff schedules with the GATT. In the Round itself, South Africa was the only sub-Saharan African country to make an offer of tariff reduction. All other countries offered average tariff bindings that were several multiples of their existing applied rates, while they made little effort to extend the coverage of their tariff bindings beyond 2% of their tariff lines. They have thus retained considerable discretion for making tariff changes. From this perspective, the opportunity offered by the Uruguay Round for African countries to shore up the credibility of their trade reform efforts was not taken up. The opportunity continues to exist, however, and is well worth pursuing in the context of more active African participation in GATT/WTO.

A third option in the search for an external agency of restraint for Africa is to have a series of African customs unions linked to the European Union in fully reciprocal free trade arrangements that would essentially replicate many of the key features of NAFTA. This scheme could provide a powerful lock-in mechanism and underpin the credibility of African trade reform since treaty commitments with this large and rich northern partner would be too costly to be repudiated by any African country. The

guarantee of access to this large market could also assist in attracting inward direct foreign investment.

This proposal raises several issues that need to be carefully examined before its viability can be established. First, it is not clear what the interest of the EU would be in such an arrangement. Second, many in Africa might regard the arrangement as a recolonization of Africa. Third, the relative costs and benefits of the arrangement should be comprehensively analysed. It is not immediately obvious that it would not impose inordinately high costs or that its potential benefits are not being overstated. The generalization from a relationship based on trade policy to the surveillance of a whole range of economic and socio-political policies, which this arrangement may encourage, could lead to the establishment of “harmonized” rules and standards that may be inappropriate for particular African country circumstances.

## **Annex. The researchers in this collaborative project**

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**Title: Regional Integration and Trade Liberalization in Sub-Saharan Africa**

Volume 1 - Framework, Issues and Methodological Perspectives

Volume 2 - Country Case Studies

Volume 3 - Regional Case Studies

Volume 4 - Synthesis and Review

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Dean de Rosa, IFPRI

- Chapter 7: A Methodology for the Study of Trade Liberalization  
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Piritta Sorsa, IMF, Geneva Office
- Chapter 10: Changing Political and Economic Conditions for Regional Integration in Sub-Saharan Africa  
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- Chapter 11: Regional Integration in Sub-Saharan Africa: Dead End or a Fresh Start?  
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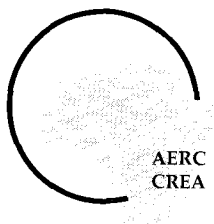


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#### **Volume 4: Synthesis**

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